

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission,)	
On Its Own Motion)	
v.)	
Commonwealth Edison Company)	
)	ICC Docket No. 12-0321
Annual formula rate update and revenue)	
requirement reconciliation authorized by)	
Section 16-108.5 of the Public Utilities Act.)	

REPLY BRIEF OF
THE PEOPLE OF THE STATE OF ILLINOIS
and AARP

The People of the State of Illinois

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The People of the State of Illinois, by LISA MADIGAN, Attorney General of the State of Illinois (the “People,” or “AG”) and AARP, through its counsel, pursuant to the Commission’s rules, 83 Ill. Admin. Code 200.800 and the schedule established by the Administrative Law Judges, file their Reply Brief in this proceeding in response to the Initial Briefs filed by the parties in response to the request by Commonwealth Edison Company (“ComEd”) to adjust its formula revenue requirements and rates pursuant to Section 16-108.5 of the Public Utilities Act (“PUA” or “the Act”).

I. INTRODUCTION

The People agree with ComEd that the Electric Infrastructure Modernization Act (EIMA), 220 ILCS 5/16-108.5, is to be applied so that ComEd’s rates are based on the utility’s *actual* costs for the applicable period. See ComEd Ini. Br. at 1. EIMA directs the Commission to determine ComEd’s actual costs by reference to ComEd’s FERC Form 1, in a manner consistent with Article IX of the Public Utilities Act to the extent they do not conflict with the Act. 220 ILCS 5/16-108.5(c). Significantly, EIMA directs that the performance-based formula

rate approved by the Commission allow recovery of ComEd's "actual costs of delivery services that are prudently incurred and reasonable in amount consistent with Commission practice and law." *Id.* at 16-108.5(c)(1). In addition, EIMA provides that "Nothing in this Section is intended to allow costs that are not otherwise recoverable to be recoverable by virtue of inclusion in FERC Form 1." *Id.* at 16-108.5(c). EIMA plainly intended the Commission to continue to apply regulatory principles of reasonableness and prudence to ComEd's statement of its "actual costs." EIMA is not a blank check.

ComEd complains that the Commission's application of the regulatory principles of reasonableness and prudence to ComEd's requested revenue requirement will result in ComEd "seriously under-recover[ing] its costs, year after year." ComEd Ini. Br. at 2. ComEd's complaint has no legal significance in this docket. ComEd witness Ross Hemphill recognized that this proceeding is properly based on "the formula tariff and other filed schedules, as established in Docket No. 11-0721. It does not consider substantive changes to the tariff and filed schedules." ComEd Ex. 8.0 at 3; ComEd Ex. 11.0 at 6-7. The Commission's determinations in Docket 11-0721 are not subject to collateral attack under EIMA.¹ ComEd has appealed the Commission's Orders in Docket 11-0721, and it is now up to the Appellate Court to determine whether, as the People believe, the Commission's decisions were fully authorized and consistent with EIMA. ComEd's unhappiness with the Commission's prior decisions is truly irrelevant to this proceeding.

¹ EIMA provides that "Subsequent changes to the performance-based formula rate structure or protocols shall be made as set forth in Section 9-201 of this Act, but nothing in this subsection (c) is intended to limit the Commission's authority under Article IX and other provisions of this Act to initiate an investigation of a participating utility's performance-based formula rate tariff, provided that any such changes shall be consistent with paragraphs (1) through (6) of subsection (c)." 220 ILCS 5/16-108.5(c).

EIMA does not impose mandatory regulatory obligations on electric utilities. Rather, it is applied at the election of the utility and remains in effect at the utility's discretion. *Id.* at 16-108.5(c). ComEd witnesses Hemphill, Trpik, and Fruehe all confirmed that ComEd will continue to operate under EIMA, and that even at the lower revenue levels allowed in Docket 11-0721, "except for certain revisions relating to the AMI deployment schedule, there is no basis for additional changes to the plan investment forecast submitted with ComEd's direct testimony." ComEd Ex. 11.0 at 9, ComEd Ex. 13.0 and ComEd Ex. 14.0. Notwithstanding ComEd's complaints in its Initial Brief, the Company is proceeding with the investment obligations, guaranteed profit collar,² annual rate review and retrospective reconciliation, and performance mandates contained in EIMA.

III. RATE BASE

C. Potentially Contested Issues

1. ADIT: Accrued Vacation Pay

ComEd argues that the AG/AARP proposed vacation pay ADIT adjustment (as well as the CUB-proposed similar adjustment) should not be accepted because "AG/AARP and CUB have essentially imputed a deferred tax liability (which reduces rate base) related to the accrued vacation pay debit when none exists." ComEd Ini. Br. at 19. The Company claims that "AG/AARP and CUB have simply incorrectly conjured one up mathematically where none exists. *Id.* at 20. The Company further asserts that the proposed adjustment is inconsistent with Section 16-108.5(c) and (d) of the Act because it does not reflect the Company's actual costs. *Id.* The record evidence, however, belies these claims. The ComEd calculation of the ADIT related to vacation pay is both flawed and inconsistent with both the Company's current state and

² See ComEd Ini. Br. at 8; ComEd Ex. 3.1, Sch. FR A-3.

federal income tax rates, as well as with the Commission's recent order in Docket No. 11-0721, ComEd's first formula rate proceeding.

The issue here is one of simple matching. Specifically, ComEd has deducted \$25,286,000 in accrued vacation pay from rate base as an operating reserve. The Company proposes to offset this amount with a deferred tax debit balance of \$18,952,000. But the deferred tax balance properly matched to an accrued reserve balance of \$25,286,000 is \$10,412,000 ($41.175\% * \$25,286,000$) – not the \$18.9 million amount ComEd proposes. The additional deferred tax debit balance of \$8,540,000 ($\$18,952,000 - \$10,412,000$) that ComEd is proposing to add to rate base is related to something other than the balance of accrued vacation pay that is deducted from rate base, and this additional \$8,540,000 is not properly includable in rate base operating reserve. ComEd Ex. 10.3, WP 5, Page 6, AG/AARP Ex. 4.0 at 2 and 4.1. Simply put, the evidence shows that Mr. Effron's adjustment limits the deferred tax debit balance included in rate base to the amount that is *consistent with the net accrued vacation pay* that is deducted from the Company's rate base. *See also* AG/AARP Initial Brief at 6-10. As such, contrary to ComEd's claims, the adjustment truly reflects ComEd's actual costs, and is completely consistent with Sections 16-108.5(c) and (d) of the Act.

The Company further claims that it has performed the calculation of the deferred income tax asset in accordance with the May 11-0721 Order. ComEd Ini. Br. at 21. That is not the case, for the reasons previously detailed in the AG/AARP Initial Brief. *See* AG Initial Brief at 9-10. As noted there, it is Mr. Effron's proposed calculation of the deferred tax debit balance to be included in rate base that is consistent with the method adopted by the Commission in Docket No. 11-0721. As shown on Appendix A, Page 7 of the May 29, 2012 Order in Docket No. 11-0721 ICC Staff Schedule 16.07R shows the adjustments to rate base related to the accrued

reserve for vacation pay and associated deferred taxes. A copy of Staff Exhibit 16.07R from Docket 11-0721 is attached to Mr. Effron's Rebuttal testimony as Exhibit 4.2 and shows the "ADIT on Reserve for Accrued Vacation per Staff" to be included in rate base as the product of the combined income tax rate and the balance of the operating reserve for accrued vacation pay that is deducted from rate base. That is precisely what Mr. Effron proposes in the present case.

In Docket No. 11-0721, the Commission did not eliminate the accrued vacation pay included in operating expenses from the rate base deduction for accrued vacation pay. ComEd is not proposing to include the product of the combined income tax rate and the rate base deduction for accrued vacation pay as the relevant deferred tax debit balance in rate base. In that regard, ComEd witness Fruehe's proposed deferred tax debit balance is not calculated in accordance with the Commission's Final Order in Docket No. 11-0721 and, as noted above, inappropriately increases the rate base used to establish the revenue requirement in this proceeding.

For all of these reasons, the Commission should reject ComEd's calculation and adopt Mr. Effron's well-supported recalculation of these ADIT amounts, which has the effect of reducing the ComEd rate base by \$8,540,000.

IV. REVENUES

C. Potentially Contested Issues

1. Billing Determinants

ComEd characterizes the \$1.8 million effect of recognizing the increased customer count resulting from plant additions in ComEd's billing determinants as "[p]erhaps the most glaring effort" to move away from cost recovery. ComEd Ini. Br. at 3. In addition to ignoring years of Commission regulatory practice to accurately match the number of customers with billing

determinants,³ ComEd's argument belies an attempt to institutionalize consistent over-recovery of its authorized revenue requirement through an under-estimate of the number of customers in the rate year. As ComEd admits, while billing determinants do not have any effect on ComEd's revenue requirement, they can change the amount of revenue which ComEd ultimately recovers and the specific rates paid by consumers because the more customers over whom to spread its total revenue requirement, the lower the individual rates. ComEd Ini. Br. at 23. If the revenue requirement is spread over too many customers, rates will be too low and if they are spread over too few customers rates, will be too high.

The Commission has consistently matched customer growth (and associated billing determinants) with ComEd's projected plant additions. ICC Docket 11-0721, Order of May 29, 2012 at 75-76. This represents application of the fundamental regulatory matching principle. Rates for the 2013 rate year are based on two components: historical costs from 2011 and projected plant additions for 2012. Of the plant additions included in rate base, approximately \$130.0 million represents facilities to accommodate customer growth. AG/AARP Ex. 2.0 at 6. The billing determinants adjustment correctly matches the 2012 projected plant additions associated with new business with the increase in the number of customers responsible for this new business investment. See also Staff Ini. Br. at 12-13. ComEd's suggestion that EIMA requires the Commission to disregard this matching principle both ignores well-established Commission practice and law and misreads the Act's treatment of billing determinants.

ComEd argues that EIMA requires the Commission to use "historical, weather-normalized billing determinants." The language in EIMA provides that the Commission shall:

³ See AG/AARP Initial Brief at 10-11, citing the Commission's orders in Docket Nos. 05-0579 and 07-0566 and 10-0467.

(4) Permit and set forth protocols, subject to a determination of prudence and reasonableness consistent with Commission practice and law, for the following: (H) historical weather normalized billing determinants.

220 ILCS 5/16-108.5(c)(4)(H). Commission practice and law requires that the number of customers counted in the historical billing determinants match the historical plant in place when rates are collected. The costs associated with 2012 plant additions associated with new business will be collected in 2013, requiring the adjustment recommended by AG/AARP witness David Effron, Staff witness Rukosuev, and CUB witness Smith.⁴ This adjustment, based on 2012 plant additions, does make these 2011-2012 billing determinants less than historical when collected in 2013.

ComEd also complains that the billing determinants adjustment does not take into account the decrease in kwh usage ComEd predicts. ComEd Ini. Br. at 25-26. This argument was disposed of by the Commission in ICC Docket 11-0721 as follows:

AG/AARP witness Effron recommended limiting the adjustment to the customer growth that is related to plant additions. He did not include the change in kwh usage, despite the fact that, in past cases, ComEd and the Commission have recognized growth in both the number of customers and kwhs, because ComEd showed a decline in weather-normalized sales. (*See*, AG/AARP Ex. 1.0 at 17).

AG/AARP aver that he did not decrease the amount of total kwhs, because plant additions for customer growth, by definition, only result in growth, otherwise, the investments for customer growth would not be made. However, in light of the overall decline in ComEd's total kwh sales, Mr. Effron did not recommend increasing the amount of total kwh sales billing determinants. AG/AARP aver that therefore, their witness, Mr. Effron, did, in fact, take into account the decrease in total kwh sales.

⁴ As indicated in the People's and AARP's Initial Brief, they accept the Staff calculation of the increased number of customers associated with the new business plant additions. AG/AARP Ini. Br. at 16.

Order at 74 (May 29, 2012). Mr. Effron's adjustment is consistent with his adjustment that the Commission adopted in that case. AG/AARP Ex. 4.0 at 5. Further, the Commission expressly rejected ComEd's argument that it was appropriate to somehow decrease the overall number of kwhs delivered when recognizing the increase in customers due to new business investment.

The Commission stated:

Additionally, a decline in kwh sales, in and of itself, does not establish that there are less customers. It simply means that less electricity was sold. Other factors, such as energy efficiency, a bad economy, etc. may very well contribute to a decline in kwh sales. Without information as to what causes a decline in kwh sales, it does not appear that this decline should offset the increase in billing determinants that reflects ComEd's new business. ComEd, in short, has not presented valid reasons for rejecting the AG/AARP proposal. The AG/AARP proposal is reasonable and it is approved. ComEd shall adjust its billing determinants accordingly.

ICC Docket 11-0721, Order at 75 (May 29, 2012). ComEd's claimed decrease in kwh sales is already incorporated into its per customer usage calculation in the billing determinants, and no further adjustment is appropriate as a result of new business. However, a decrease in usage per customer does not mean that there is a decrease in *the number of customers*, particularly when ComEd has identified \$130 million in plant additions for new business for 2012, the year prior to the rate year (2013).

The People and AARP request that the Commission adjust ComEd's revenue requirement to incorporate the new business adjustment and correct the billing determinants accordingly.

V. OPERATING EXPENSES

C. Potentially Contested Issues

1. Administrative and General Expenses

d. Merger Costs

Given the fact that the merger between ComEd's parent Exelon and Constellation Energy Group was not closed until March of 2012, it is clear that in 2011 there were no merger savings – only merger-related costs. ComEd argues that Illinois's ComEd customers should shoulder these pre-merger costs incurred *in anticipation* of future merger-related savings. ComEd Ini. Br. at 42. The Company admits that these costs were incurred to integrate the two parent companies (Exelon and Constellation) on “day one” and that these pre-closing costs were “a step necessary” to facilitate anticipated future savings. *Id.* at 44, 46.

ComEd cites its witnesses' testimony describing the amount of anticipated merger savings by 2015 and the procedures Exelon put in place to track its “integration” efforts. While these promises are potentially laudable, they do not address the fact that in the two jurisdictions that reviewed the merger, Exelon and Constellation proposed that no merger costs be collected from consumers except to the extent that the costs are offset by merger savings. See “Order Conditionally Authorizing Merger and Disposition of Jurisdictional Facilities” at page 40-42, 138 FERC 61,167 (Issued March 9, 2012) (discussed in the AG/AARP Initial Brief at 21) and *In the Matter of the Merger of Exelon Corporation and Constellation Energy Group*, Case No. 9271 at 8a4-85 (Feb. 17, 2012) (CUB Ex. 2.1) (discussed in the AG/AARP Initial Brief at 22). No matter how many integration processes are in place or how many savings are predicted, allowing recovery of costs in the absence of contemporaneous savings adversely affects rates.

Section 7-204 of the Public Utilities Act requires that reorganizations that result in a change in ownership of a public utility are subject to Commission approval. 220 ILCS 5/7-204(a). ComEd did not present the Exelon/Constellation merger to the Commission under this section, so that Commission did not review it to assure that there were no “adverse rate impacts on retail customers.” *Id.* at 7-204(b)(7). However, the two jurisdictions that did review the

merger concluded that the Companies' offer to hold customers harmless for five years (before the Federal Energy Regulatory Commission) and assurance that the transaction would be "rate neutral" (before the Maryland Public Service Commission)⁵ protected consumers from adverse rate impacts. It is reasonable for Illinois consumers to have the same protections against rates increasing as a result of merger costs that have not yet led to merger related savings.

ComEd cites the Commission decision in ICC Docket 05-0597 for the proposition that the Commission has allowed ComEd to recover costs related to savings plans in the past.

ComEd Ini. Br. at 48. A review of the Commission's decision in that docket demonstrates that the savings for which cost recovery was allowed were already being realized in the test year.

The Commission stated: "The record is clear that there are already savings from the Exelon Way program that will be reflected in the rates in this proceeding. In addition, no party has disputed that, as a result of Exelon Way, at least 70 million dollars a year in savings are expected." ICC Docket 05-0597, Order at 90 (July 26, 2006)(severance costs of \$21 million claimed).

ComEd also cites Commission rule 285.3215(a) as allowing "recovery of costs incurred in a 'test year' related to a cost savings program that is anticipated to result in future jurisdictional costs savings." ComEd Ini. Br. at 48. That rule describes the information to be included in Schedule C-22, entitled "Cost Savings Programs" and is reproduced in the footnote in its entirety.⁶ If ComEd intended this section to justify its merger costs, it failed to include any

⁵ See AG/AARP Initial Brief at 20-21 quoting the relevant orders.

⁶ **Section 285.3215 Schedule C-22: Cost Savings Programs**

a) Provide information concerning any cost savings program that is anticipated to result in annual jurisdictional savings in excess of the lesser of \$1,000,000 or .1% of operations and maintenance expenses in the year preceding the initiation of the program and whose initial costs are sought to be recovered in the test year.

b) Information provided shall include:

- 1) Title;
- 2) Description;
- 3) Date of implementation;
- 4) Initial start up costs to implement program;
- 5) Costs to be incurred for each year of the next three years; and

information on the Schedule C-22 it filed with this docket, as shown in Attachment 1 to this Reply Brief. ComEd cannot rely on this section of the Commission's rules or the Order in ICC Docket 05-0597 to justify including merger-related costs in its rev req because it did not submit any information in its Schedule C-22 and because in the rate order, savings were being realized in the test year to justify the recovery of associated expenses.

Notwithstanding ComEd's claims of anticipated, future merger-related savings, it is not reasonable to expect Illinois consumers to pay the costs of "day one" integration of Exelon and Constellation, particularly when Exelon's ownership of ComEd did not change in the test year.⁷ Further, the jurisdictions that have reviewed the merger to assure that consumers are not harmed or adversely affected have both limited the recovery of merger-related costs to the extent of savings. Finally, the Commission's Order in ICC Docket 05-0597, cited by the Company, involved savings in the test year period that exceeded the costs. These precedents all support the conclusion that it is simply not reasonable to expect Illinois consumers to bear these costs prior to the closing of the transaction and without regard to coincident savings. The People and AARP request that the Commission adjust ComEd's reconciliation balance and inception rates to remove costs associated with the merger of Exelon and Constellation Energy Group.

VIII. OTHER

C. Potentially Contested Issues

3. a. Identification of Costs Incurred in Compliance with Section 16-108.5

ComEd argues that it cannot practically identify the investments that are EIMA related because they are rolled into ComEd's total investment during the ten year investment period.

6) Annual savings expected for each of the next three years.
83 Ill. Admin. Code 285.3215.

⁷ Given ComEd's decision not to seek approval of the transaction under Section 7-204 of the Public Utilities Act, it is apparent that ComEd did not expect a change in ownership necessitating "day 1" changes because ComEd is still owned by Exelon. ComEd witness Jirovec testified that there was no reduction in employees or labor expense related to the merger in 2011 or on Day 1, which in any event was not in 2011. Tr. at 124, Line 15 to 125, Line 7.

ComEd Ini. Br. at 62-63. ComEd's position is curious, given the requirement that it file annual reports with the Commission that "shall include a schedule and staffing plan for the next calendar year." While the infrastructure plan required by Section 16-108.5(b) "need not allocate the work equally over the respective periods, [it] should allocate material increments throughout such periods commensurate with the work to be undertaken." 220 ILCS 5/16-108.5(b).

ComEd's assertion that it is "impracticable to take individual investments and basically paint them as to whether they are EIMA or not"⁸ is simply not credible in light of the Company's obligation to file an annual report identifying and scheduling the \$2.6 billion of incremental investment over 10 years. The People and AARP agree with the Staff that "the notion that it is impossible to provide this information is belied by the evidence in this proceeding." Staff Ini. Br. at 38-39.

ComEd asserts that it "cannot identify specific 'incremental' investments of their costs" or judge what investments would or would not have been made in the absence of its election to be a participating utility. ComEd Ini. Br. at 62. In addition to the fact that ComEd is obligated to file annual reports specifying its investments pursuant to the Act, the entire premise of EIMA is that the utility receives special ratemaking treatment in return for making specific types of investments in specific dollar amounts. These investments are in addition to "business as usual" and EIMA provides special ratemaking treatment to assure that they are made.

EIMA also authorizes the Commission to assure that the EIMA investment costs are "prudent and reasonable." Section 16-108.5(b-5) provides:

Nothing in this Section shall prohibit the Commission from investigating the prudence and reasonableness of the expenditures made under the infrastructure investment program during the annual review required by subsection (d) of this Section and shall, as part of such investigation, determine whether the utility's

⁸ ComEd Ini. Br. at 62.

actual costs under the program are prudent and reasonable. The fact that a participating utility invests more than the minimum amounts specified in subsection (b) of this Section or its plan shall not imply imprudence or unreasonableness.

220 ILCS 5/16-108.5(b-5). This subsection references subsection (d), which requires the utility to file “updated cost inputs to the performance-based formula rate” each year by May 1.

Clearly, if the Commission is to include a review of the Company’s infrastructure investments “during the annual review required by subsection (d)” information about the infrastructure investments and costs must be available to the Commission.

ComEd is under an obligation to know that it is spending an incremental \$1.3 billion over five years on “electric system upgrades, modernization projects, and training facilities,” including an estimated \$1 billion for underground residential cable and mainline cable system refurbishment and replacement, an estimated \$10 million for training facilities, an estimated \$200 million for storm hardening, and investment in “wood pole inspection, treatment and replacement.” 220 ILCS 5/16-108.5(b)(1)(A)(i)-(iv). It must also track \$1.3 billion of investment “to upgrade and modernize its transmission and distribution infrastructure and in Smart Grid electric system upgrades” over a ten year period. *Id.* at 16-108.5(b)(1)(B)(i)-(iv). The Commission and the public are entitled to know that these investments are being made, what the investments specifically are, and the costs associated with the required investment categories. ComEd’s obligations under EIMA extend to more than simply investing more money: it must invest money in certain types of infrastructure and its investments must be transparent. See 220 ILCS 5/16-108.5(c)(formula “to operate in a standardized manner and be updated annually with transparent information.”).

The People and AARP continue to support the Staff recommendation that ComEd identify its EIMA infrastructure investments in its Annual Performance-Based Formula Rate filing. See Staff Ini. Br. at 40-41.

IX. CONCLUSION

For the foregoing reasons, the People of the State of Illinois and AARP request that the Commission issue an order consistent with the positions stated above.

The People of the State of Illinois

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